No. 82-999

IN THE

Supreme Court of the United States

OCTOBER TERM, 1982

CHEMETRON CORPORATION,
Petitioner,

v.

BUSINESS FUNDS, INC., JOHN F. AUSTIN, JR., AND DAVID C. BINTLIFF,
Respondents.

BRIEF OF RESPONDENTS IN OPPOSITION TO PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

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January 17, 1983

QUESTION PRESENTED

Whether the failure by plaintiff to satisfy the congressionally mandated substantive elements of a securities manipulation claim under section 9(e) of the Securities Exchange Act may be obviated by substitution of an implied cause of action under section 10(b)?

RULE 28.1 STATEMENT

The parents, subsidiaries, and affiliates of Business Funds, Inc. are Penn Central Corporation and Marathon Manufacturing Company.

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Cases

Statutes

Rules and Regulations

Abbreviations

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STATEMENT OF THE CASE

Petitioner, Chemetron Corporation, acquired shares in Western Equities, Inc. ("Westec") in a negotiated, off-market transaction through an exchange of stock by Westec for the assets of a Chemetron subsidiary.[1] Chemetron paid fourteen dollars ($14.00) per share at a time when the prevailing market price was forty-seven dollars ($47.00) per share. *Chemetron Corp.* v. *Business Funds, Inc.*, 682 F.2d 1149, 1187 (5th Cir. 1982), A75; Pltfs. Tr. Ex. 298. When Westec was forced into bankruptcy months after the transaction, Chemetron filed suit to recoup

[1] The facts relevant to the question presented are well stated by the Fifth Circuit. *Chemetron Corp.* v. *Business Funds, Inc.*, 682 F.2d 1149, 1153-55 (5th Cir. 1982), A1-A6. Citations to Petitioner's Appendix are designated A.. or B.. as appropriate.

losses it allegedly sustained on its investment. Chemetron alleged that Respondents illegally manipulated the national securities exchange market for Westec stock and failed to disclose or made misleading statements with regard to the manipulative scheme. It attempted to recover based on two distinct causes of action under the federal securities laws: (1) the express remedy set forth in section 9(e) of the Securities Exchange Act of 1934, 15 U.S.C. § 78i(e), in favor of a purchaser of a security whose price has been affected by certain kinds of manipulation, and (2) the remedy implied pursuant to section 10(b) of the Securities Exchange Act, 15 U.S.C. § 78j(b), and Rule 10b-5, 17 C.F.R. § 240.10b-5.[2]

Thirty-one special interrogatories were submitted to the jury at the conclusion of a six-week trial. The jury specifically determined that an explicit substantive element of the express section 9 remedy had not been established; the alleged manipulation had not "affected" the price paid by Chemetron for its Westec stock. B3. This finding was consistent with the uncontroverted testimony of the Chemetron executive who negotiated the transaction that Chemetron was "not influenced by the market" and that market prices had nothing to do with the "fundamental values" involved. 682 F.2d at 1186-87, A75; Tr. 2305, 2226, 2245.

Despite the jury's finding, the district court entered a judgment of joint and several liability for $18,413,160 against

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[2] Chemetron also sought to recover under the Texas fraud statute, TEX. REV. CIV. STAT. ANN. art. 4004 (Vernon 1966) [current version at TEX. BUS. & COM. CODE § 27.01 (Vernon 1968)]. The district court's determination of certain state law issues was reversed and remanded by the court of appeals for a new trial. 682 F.2d at 1194, A92. Hence, regardless of the Court's disposition of the petition, this case will require remand to the district court for further proceedings. Indeed, should the petition be granted and the case reversed with regard to the federal securities law issue, the case would require remand to the court of appeals for further consideration, since the court of appeals pretermitted "discussion of numerous other issues raised on appeal insofar as they are directed at the federal securities law claims." *Id.* at 1170 n.56, A36 n.56.

Respondents under section 10(b) and Texas law. Chemetron moved for judgment notwithstanding the verdict as to the section 9(e) claim, which was denied, as were the motions of Respondents for judgment notwithstanding the verdict under section 10(b) and for a new trial. The Respondents appealed and Petitioner cross-appealed. The United States Court of Appeals for the Fifth Circuit reversed the district court's judgment under section 10(b) and under Texas law and rejected Chemetron's cross-appeal except as to the application of collateral estoppel to David C. Bintliff. (This holding is the subject of the conditional cross-petition for a writ of certiorari filed by David C. Bintliff.)

Based on a careful review of this Court's decisions, the Fifth Circuit, in an opinion by Judge Gee, concluded that the question before it was "whether permitting a Rule 10b-5 action here will impermissibly broaden the section 9 remedy by nullifying its restrictions in defiance of the congressional mandate." 682 F.2d at 1159, A13. It compared subsection 9(a)(4) (misrepresentation/nondisclosure) with the similar prohibitions in Rule 10b-5(b), and compared subsections 9(a)(1), (2) and (6) (bans on specific stock manipulation schemes) with the general bans on fraudulent schemes and courses of business in Rule 10b-5(a) and (c). 682 F.2d at 1158, A11. In an analysis that even the dissenter was forced to concede was "meticulously reasoned," *id.* at 1194, A93, the court concluded that in each instance the Rule 10b-5 remedies created a lower burden of proof and would concomitantly enlarge the plaintiff class. 682 F.2d at 1160-65, A17-A26. It determined that the creation of a broader and less rigorous judicial remedy under Rule 10b-5 would nullify the more restrictive statutory remedies created by Congress in section 9. The court thus found it improper to imply a remedy for Chemetron under Rule 10b-5.

The court held its conclusion consistent with its analysis in *Huddleston* v. *Herman & MacLean*, 640 F.2d 534 (5th Cir.), *modified on denial of rehearing*, 650 F.2d 815 (5th Cir. 1981), *cert. granted*, 102 S. Ct. 1766 (1982), in which a remedy was

determined to be implied appropriately under Rule 10b-5 because such actions require a higher burden of proof than those based on sections 11 and 12(2) of the 1933 Act, 15 U.S.C. §§ 77k & 77*l*(2) (1976). 682 F.2d at 1159-60, A15-A16.

Finally, the court decided that its conclusion that section 9 was an exclusive remedy in this case was reinforced by an exhaustive analysis of the legislative history of section 9. 682 F.2d at 1165-69, A27-A36.

REASONS FOR DENYING THE WRIT

Chemetron ignores the Fifth Circuit's analysis of the question presented to this Court. It takes no issue with the demonstration that the implication of a section 10(b) remedy requiring a lesser burden of proof and creating a broader class of plaintiffs would nullify Congress' deliberate and careful limitations on the express statutory remedies of section 9. Nor does Chemetron challenge the court's exhaustive analysis of the legislative history.

The central thrust of Chemetron's petition is a rhetorical argument that the Fifth Circuit's decision will leave little of Rule 10b-5 and do "grievous harm to the prime legislative objective of cleansing the Nation's securities markets of manipulative influences." Petitioner's Br. at 10-11. Chemetron offers no substantiation for such rhetoric and there is none. Even assuming the validity of Chemetron's claims of market manipulation, every purchaser who bought on the market actually affected would have a remedy under section 9. Indeed, Chemetron itself would have had a remedy but for the circumstance that, under the highly peculiar facts of this case, it bought at a price not affected by any market manipulation.[3]

The Fifth Circuit decision does not limit the section 9 remedy but only recognizes that a necessary element of the claim was

[3] Chemetron does not attempt to support its assertion that § 9 was improperly construed by the courts below. As the Fifth Circuit demonstrates, the point is meritless. 682 F.2d at 1186-87, A74.

not established at trial. In this case Chemetron simply failed to sustain its burden of proof. Nor does the Fifth Circuit's decision detract from the vitality of the implied remedy under section 10(b) in appropriate circumstances. It did not infringe on the remedial, "catch-all" purpose of section 10(b) when there is a true gap in the securities laws. Nor did it limit access to the section 10(b) remedy in cases in which statutory restrictions adopted by Congress would not be nullified.

Chemetron's entire petition speaks as if the Court's securities decisions of the past decade, with their emphasis on congressional language and intent and their refusal to permit nullification of express remedies by less rigorous implied remedies, do not exist. Chemetron continues to assume, contrary to this Court's decisions, that every violation of federal law is entitled to a private remedy[4] regardless whether Congress intended such a result. *See Touche Ross & Co.* v. *Redington*, 442 U.S. 560, 568 (1979). Arguing from a perspective it asserts to be one of policy, Chemetron simply does not deal with the prevailing legal standards. Yet, as the Court has stated, "The ultimate question is one of congressional intent, not one of whether this Court thinks it can improve upon the statutory scheme that Congress enacted into law." *Id.* at 578.

Chemetron's suggestion that decision on its petition should be delayed pending this Court's decision in *Huddleston* is unwarranted. The Fifth Circuit's analysis demonstrates that its decision in this case is consistent with affirmance of *Huddleston*. Should this Court reverse *Huddleston*, and hold that sections 11 and 12(2) of the 1933 Act, 15 U.S.C. §§ 77k & 77*l* (2) (1976), are exclusive remedies, then it would follow *a fortiori* that certiorari should be denied in this case.

We shall deal briefly with Chemetron's specific points that are predicated on the "worst scenario" from its perspective — reversal of *Huddleston*.

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[4] Petitioner still has available a claim under state law for the same conduct on which the federal securities law claims were based.

First, Chemetron's attempt to characterize *Huddleston* as involving questions of express and implied remedies, while this case involves two distinct violations is without force. All that is at issue here is whether there is an implied private remedy in addition to and less rigorous than the express statutory private remedy. Reliance by Chemetron upon cases concerning government power to bring enforcement proceedings is inappropriate because such cases present an entirely distinct question. This point is made in *United States* v. *Naftalin*, 441 U.S. 768 (1979), the very case on which Chemetron principally relies. In upholding a conviction under section 17(a)(1) of the Securities Act of 1933, the Court pointed out that *Blue Chip*[5], involving a private implied cause of action, was "inapplicable" to a criminal prosecution. 441 U.S. at 774 n.6.[6]

Second, *SEC* v. *National Securities, Inc.*, 393 U.S. 453 (1969), in addition to being a government enforcement case, treated only the question of the relationship of section 14 of the 1934 Act, 15 U.S.C. § 78h, and Rule 10b-5. 393 U.S. at 468. Nothing in its analysis is inconsistent with or suggests a different result in this case. The Fifth Circuit did not suggest that all statutory remedies are exclusive; *National Securities* does not imply that other statutory remedies may not be exclusive.

Third, the isolated appellate decision of *Schaefer* v. *First National Bank of Lincolnwood*, 509 F.2d 1287 (7th Cir. 1975), *cert. denied*, 425 U.S. 943 (1976), does not establish a meaningful conflict between courts of appeals. *Schaefer* was decided eight years ago, before this Court's decisions in cases such as

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[5] *Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 723 (1975).

[6] Thus the fact that dual criminal prosecutions were involved in the Westec collapse is irrelevant. Parallel criminal charges are brought on the basis of express statutory provisions making the conduct criminal. Criminal charges may be brought for willful violations of § 11 pursuant to § 24 of the 1933 Act, 15 U.S.C. § 77x, and charges can be brought for willful violations of § 9(a) and § 10(b) pursuant to § 32 of the 1934 Act, 15 U.S.C. § 78ff.

Touche Ross,[7] *Blue Chip*,[8] *Hochfelder*,[9] *Chiarella*,[10] and *Transamerica*,[11] which emphasize the importance of congressional intent and recognize that implied remedies may not nullify congressionally imposed restrictions. Decisions in the Seventh Circuit acknowledging the learning of this Court's subsequent decisions indicate that *Schaefer* has been eroded as precedent even in that circuit. *See O'Brien* v. *Continental Illinois National Bank & Trust Co.*, 593 F.2d 54, 62-63 (7th Cir. 1979); *Sanders* v. *John Nuveen & Co.*, 554 F.2d 790, 794-95 (7th Cir. 1977). *See also Ross* v. *A. H. Robins Co.*, 607 F.2d 545, 554 (2d Cir. 1979), *cert. denied*, 446 U.S. 946 (1980) (criticizing *Schaefer* as "overly broad" in light of this Court's subsequent decisions).

The remainder of Chemetron's points — the nonapplicability of section 9 to over-the-counter markets, the delay of the legislative process in adoption of the American Law Institute's Federal Securities Code, the characterization of the Court's decisions in *Blue Chip*, *Hochfelder*, and *Chiarella* as a "pendulum effect," and the argument that "manipulation" is a question of federal law — do not touch the Fifth Circuit's persuasive analysis.

Chemetron does not and cannot deny that to imply a remedy under Rule 10b-5 in this case would nullify the deliberately limited remedies of section 9. It can show neither the need nor a legitimate basis for such a nullification.

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[7] *Touche Ross & Co.* v. *Redington*, 442 U.S. 560 (1979).

[8] *Blue Chip Stamps* v. *Manor Drug Stores*, 421 U.S. 723 (1975).

[9] *Ernst & Ernst* v. *Hochfelder*, 425 U.S. 185 (1976).

[10] *Chiarella* v. *United States*, 445 U.S. 222 (1980).

[11] *Transamerica Mortgage Advisors, Inc.* v. *Lewis*, 444 U.S. 11 (1979).

CONCLUSION

The petition for a writ of certiorari should be denied.

Respectfully submitted,

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CERTIFICATE OF SERVICE

Pursuant to Sup. Ct. R. 28.5, I have served all parties required to be served with three copies of the foregoing Brief of Respondents in Opposition to Petition for a Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit by placing the same in the United States mail, with first class postage prepaid and addressed to the following:

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Dated this 17th day of January 1983.

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